

# OVERSIGHT DIVISION

## Second Injury Fund Addendum

Prepared for the Committee on Legislative Research  
by the Oversight Division

Mickey Wilson, CPA, Director

Review Team: Steve Shiery, CPA, Team Leader, Jeani Hancock



COMMITTEE ON LEGISLATIVE RESEARCH  
OVERSIGHT DIVISION

September 10, 2008

Members of the General Assembly:

The Joint Committee on Legislative Research adopted a resolution in May 2007, directing the Oversight Division to perform a program evaluation of the Department of Labor and Industrial Relations, Second Injury Fund to determine and evaluate program performance in accordance with program objectives, responsibilities, and duties as set forth by statute or regulation. The program evaluation report was issued in January 2008 after its release was approved by the Joint Committee on Legislative Research.

Since the release of that report, various legislative committees have requested and received information and testimony from state agencies involved with the program. There have also been legislative changes and court decisions which would impact the program. Oversight was requested to update our evaluation of the program, review the legislative history of funding provisions for the Second Injury Fund, and consider whether changes to our report would be indicated as a result of this updated information. Based on our review of the information provided at the hearings and the additional review we have performed, Oversight does not believe the decision to increase the maximum lump sum payment amount was adequately evaluated by the Office of the State Treasurer and the Office of the Attorney General before its adoption.

Oversight analyzed the statutory provisions for funding the Second Injury Fund from 1980 to the present, and our comments on those provisions are presented on page 2. Oversight also reviewed the administrative change, made by the Office of the State Treasurer and the Office of the Attorney General in 2001, to the maximum lump sum payment amount. As noted on page 3 we were not provided complete information regarding that change by the Office of the State Treasurer and the Office of the Attorney General. Our comments related to that change are presented on page 4. In addition, Oversight reviewed certain events subsequent to the release of our report, and our comments are presented on page 5. Finally, Oversight has provided updated financial and statistical information for the program.

We hope this information is helpful and can be used in a constructive manner for the betterment of the state program to which it relates. You may request a copy of this update from the Oversight Division by calling (573) 751-4143.

Respectfully,

A handwritten signature in black ink, appearing to read "Mickey Wilson". The signature is fluid and cursive, with the first name "Mickey" and last name "Wilson" clearly distinguishable.

Mickey Wilson, CPA  
Director

## History of Second Injury Fund Revenue Provisions

### The Division of Workers' Compensation

The Missouri General Assembly first approved a workers' compensation law in 1919, although final voter approval was not completed until 1926. The Department of Labor and Industrial Relations - Division of Workers' Compensation (DWC) administers programs to implement the workers' compensation law. DWC operations are funded by a tax on employers' net workers' compensation insurance premiums and on calculated equivalent premiums for self-insured employers.

### The Second Injury Fund

The General Assembly added the Second Injury Fund (SIF) program to the Division of Workers' Compensation in 1943 to help disabled workers find employment. The revenue sources for the Second Injury Fund have been changed several times during the program's existence as noted in the following sections.

#### Premium Tax

Prior to 1987, part of the funding for the Division of Workers' Compensation and the Second Injury Fund was provided on a combined basis by a tax on net deposits or net premiums received for workers' compensation programs in Missouri, at the rate of three percent. The tax due was assessed by the Director of the Division of Insurance and based on insurance premiums, deposits, and assessments reported by insurance carriers and self-insurers. The premium reports, tax assessments, and payments were made on an annual basis until 1983 when a statutory provision for quarterly payments was enacted. An additional one percent premium tax was added for the support of the Second Injury Fund in 1987; however, this provision was repealed in 1988.

#### Workers' Compensation Tax

Tax revenues were allocated between the Division of Workers' Compensation and Second Injury Fund programs. Eighty percent of the taxes collected was allocated to the Division of Workers' Compensation, and twenty percent was allocated to the Second Injury Fund. In 1986, the allocation of funds to the Second Injury Fund was changed from twenty percent of taxes collected to thirty percent. In 1987, the taxable base was expanded from "net deposits or net premiums" to "net deposits, net premiums or net assessments" and a premium tax of one percent was added for the support of the Second Injury Fund. In 1988, the workers' compensation tax allocation to the Second Injury Fund was eliminated.

### Surcharge

Separately, revenue for the Second Injury Fund has been provided by a surcharge on premiums paid for workers' compensation insurance policies and deposits to self-insurance programs. Prior to 1986, this surcharge was limited to one-half of one percent. In 1986 the surcharge limit was increased to one percent, and in 1988 the surcharge limit was increased to three percent of net deposits, net premiums or net assessments. Additional statutory changes were made in 1993 and 2005, but the limit remained at three percent.

### Annual Rate Setting Provisions

The director of the Division of Workers' Compensation (DWC) is required to estimate the amount of benefits payable from the Second Injury Fund during the ensuing calendar year and calculate the total amount of surcharge, subject to the statutory limit, to be imposed during the ensuing calendar year on workers' compensation policy holders and self-insurers. This process results in revenue on a "pay-as-you-go" basis. Other examples of programs financed on this basis are the federal Social Security system, and Missouri local government operations.

**Oversight** recommends the General Assembly determine the proper basis for funding the Second Injury Fund program.

### Actuarial Study Requirement

In 1987, the General Assembly enacted a requirement for an actuarial study to determine the solvency of the fund and the appropriate funding level of the fund, and to forecast future expenditures from the fund. The first actuarial study was to be completed by July 1, 1988, and the study was to be repeated every three years. The legislation did not specify a basis for measuring the fund's solvency, nor for determining the appropriate funding level or forecasting expenditures. Further, the statutory provisions for rate setting were not changed to allow or require the DWC to implement any recommendations which might result from an actuarial study. The DWC did not contract with independent professional actuary firms; rather, DWC staff prepared the studies.

**Oversight** notes that the actuarial study requirement has not been linked to the rate setting requirement. As we noted above, the DWC has been directed to set the premium tax rate based on past and anticipated future revenues subject to a statutory limit. If the General Assembly determines that the funding should be on an actuarially sound basis, a professional actuarial study should be obtained. That actuarial study may result in recommendations and/or guidance to the General Assembly on any statutory changes which may need to be made.

### Change in the Maximum Lump Sum Payment and its Impact on the Second Injury Fund

In 2001, the Office of the State Treasurer (STO) and the Office of the Attorney General (AGO) increased the maximum lump sum settlement amount from \$40,000 to \$60,000. Section 287.220.2 RSMO gives the STO, with the advice and consent of the AGO, the authority to enter into compromise settlements with claimants. There do not appear to be any specific statutory limitations on the authority of the STO and the AGO to make such settlements.

Oversight was not provided any specific documentation in support of the decision to increase the maximum settlement amount; however, in response to committee requests, the AGO provided an actuarial report dated June 6, 2001 in support of this decision. The AGO did not provide a request for proposal nor a contract for the actuarial report.

Oversight's review of this administrative change in the Second Injury Fund program was limited since the RFP and contract were not provided; further officials from the AGO did not respond to our requests for additional information during this review. Oversight was not able to determine the terms under which the actuarial study was performed nor whether a subsequent actuarial review, or other form of analysis, was conducted on the impact of the increase in the maximum lump sum settlement amount. Accordingly, Oversight's understanding of the report is limited to the content of that June 6, 2001 report itself.

Oversight assumes that the change in the maximum lump sum payment amount could be a contributing factor, along with other statutory changes in the Workmens' Compensation and Second Injury Fund programs, in the reduction of the Second Injury Fund balance over recent years.

#### Short Term Impact

The Executive Summary of the report indicated that there would be additional short-term cash payments from the Second Injury Fund as a result of the increased maximum lump sum, and estimated that additional payments due to the change would amount to \$3,520,000 to \$6,000,000. Oversight was not able to determine how the amount of estimated additional payments was calculated. The actuaries concluded that the additional short-term payments "will likely stop, and could possibly reverse, the process of asset accumulation" in the fund.

#### Long Term Impact

The Executive Summary also included a set of comments by the actuaries as to the long term effect of the increased lump sum settlement limit. First, the actuaries stated they expected the increase to have a "positive impact" on the fund's overall claim costs. Second, the actuaries stated they could not quantify the point at which additional expenditures for lump sum claim settlements would be offset by reduced payments for future benefits. Finally, the actuaries stated that additional future cash disbursements due to the increased settlement limit should be less than the estimated additional expenditures for the first year after the change in the settlement limit.

The STO and the AGO apparently increased the maximum lump sum settlement limit based on their belief that the increased short-term expenditures would be more than offset by reduced future expenditures. As we noted above, we did not receive any response from the AGO regarding the actuarial study, and we have not been provided any information regarding the impact of that change. Oversight believes that an actuarial review to evaluate the impact of that change or a comparison of lump sum payments made since the change in the maximum lump sum payment limit with the amount of monthly benefits that would have been paid in the absence of those larger lump sum settlements would allow an objective analysis of the impact of the increased lump sum payment limit on the Second Injury Fund.

In our report on the program evaluation, based on the information available at the time, we had commented that an even higher lump sum payment limit might benefit the program. However, as we have noted above, significantly more analysis of such program changes should be done before such decisions are made and the impact of such changes should be evaluated on an ongoing basis.

**Oversight** recommends the General Assembly consider requesting an independent analysis of the impact of larger lump sum settlement payments on Second Injury Fund expenditures, and take appropriate action.

#### Subsequent Events

Since the Oversight Division issued its report on the Second Injury Fund in January 2008, there have been some significant events related to the Second Injury Fund.

A. As shown on Schedule 3, the balance in the Second Injury Fund has been reduced to \$19,866,107 at June 30, 2008. Expenditures exceeded revenues by \$3.47 million and \$10.0 million during the fiscal years ended June 30, 2007 and 2008.

B. As shown on Schedule 5, the number of cases filed, the number of cases dismissed, and the number of cases served have declined slightly during the two years prior to June 30, 2008. As shown on Schedule 6, the number of cases open has been reduced from a peak of 33,981 on December 31, 2005, to 27,827 on June 30, 2008.

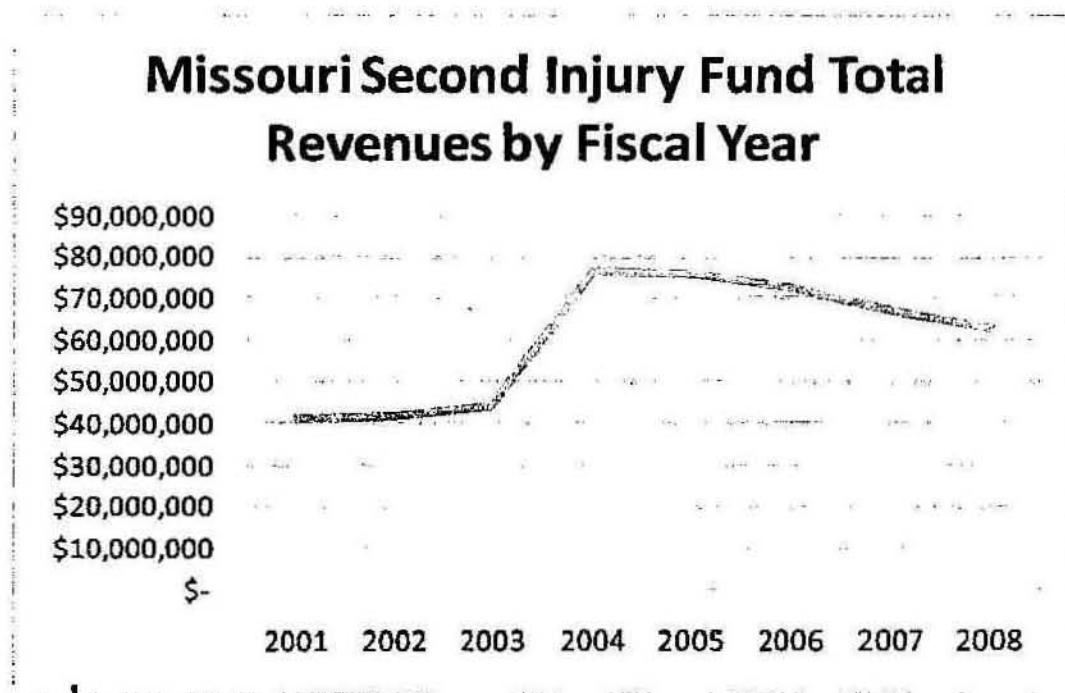
C. Hearings were conducted by the Interim Committee on the Second Injury Fund and by the Oversight Committee. Testimony was requested from the Office of the State Auditor, the Office of the Attorney General, the Office of the State Treasurer, the Department of Labor and Industrial Relations, and the Division of Workers' Compensation. Complete information on written testimony from those hearings was not available to the Oversight Division.

D. The decision by the Missouri Supreme Court in Schoemehl vs Treasurer had increased potential future benefits payable from the fund by making dependents of some claimants eligible for benefits after the death of the original claimant. The General Assembly passed, and the Governor signed HB 1883 in 2008. This proposal indicated the General Assembly's intent to reject and abrogate the Missouri Supreme Court decision.

**Oversight** recommends the General Assembly continue to monitor the status of the Second Injury Fund and take appropriate action should it become necessary.

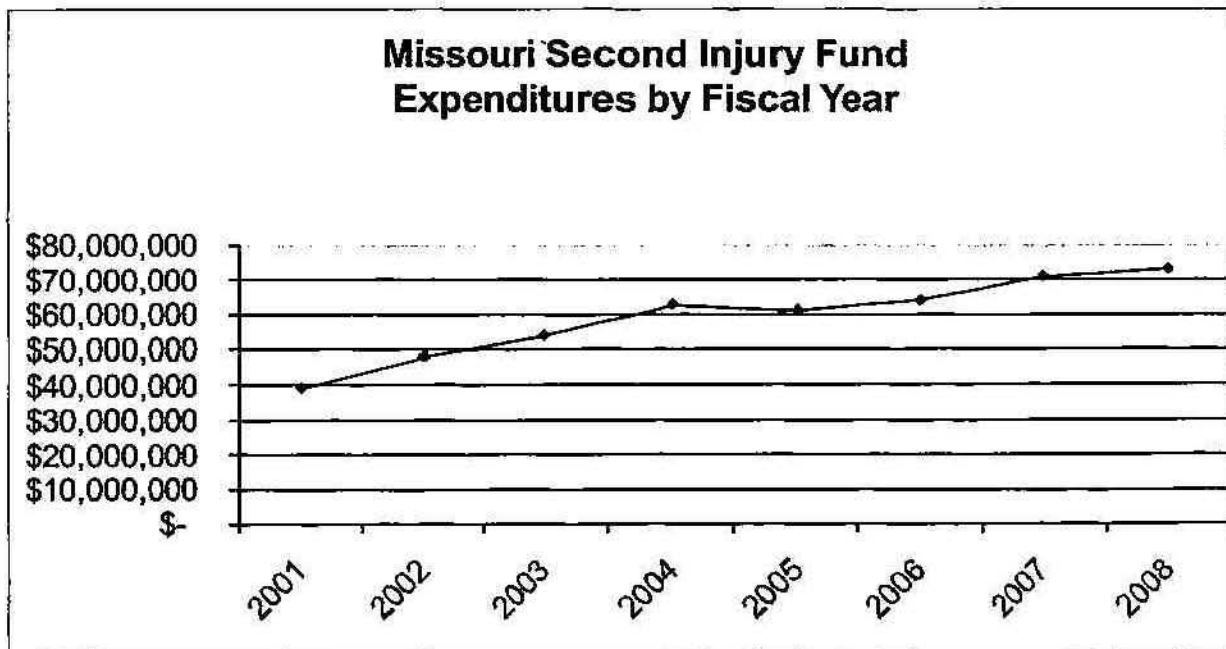
**Missouri Second Injury Fund  
Total Revenues by Fiscal Year**

<u>Fiscal Year</u>	<u>Second Injury Fund Revenues</u>
2001	\$ 41,445,642
2002	\$ 42,148,242
2003	\$ 44,121,644
2004	\$ 76,331,539
2005	\$ 76,024,241
2006	\$ 72,505,769
2007	\$ 67,024,273
2008	\$ 62,945,039



**Missouri Second Injury Fund  
Expenditures by Fiscal Year**

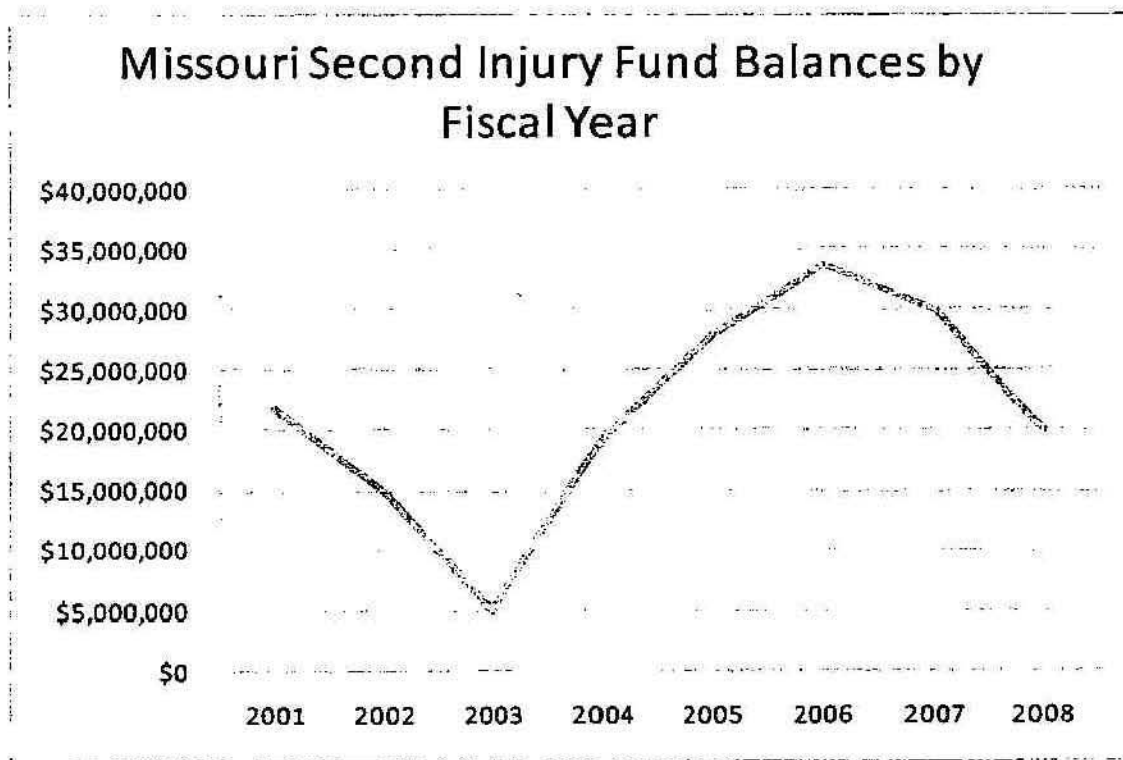
1943-1985	\$ 24,747,360
1986	\$ 7,982,201
1987	\$ 11,793,975
1988	\$ 12,540,368
1989	\$ 8,847,191
1990	\$ 19,210,378
1991	\$ 32,441,827
1992	\$ 21,746,103
1993	\$ 7,402,379
1994	\$ 18,519,292
1995	\$ 21,259,063
1996	\$ 21,705,665
1997	\$ 22,715,314
1998	\$ 25,049,419
1999	\$ 26,409,666
2000	\$ 29,389,211
2001	\$ 39,045,790
2002	\$ 47,747,639
2003	\$ 53,761,833
2004	\$ 62,546,301
2005	\$ 60,958,693
2006	\$ 63,877,107
2007	\$ 70,788,734
2008	\$ 72,927,263



## Schedule 3

Missouri Second Injury Fund  
Fund Balances by Fiscal Year

<u>Year</u>	<u>Fund Balance</u>
2001	\$21,760,262
2002	\$15,020,514
2003	\$1,854,698
2004	\$19,431,797
2005	\$27,862,916
2006	\$33,599,056
2007	\$29,837,183
2008	\$19,866,107

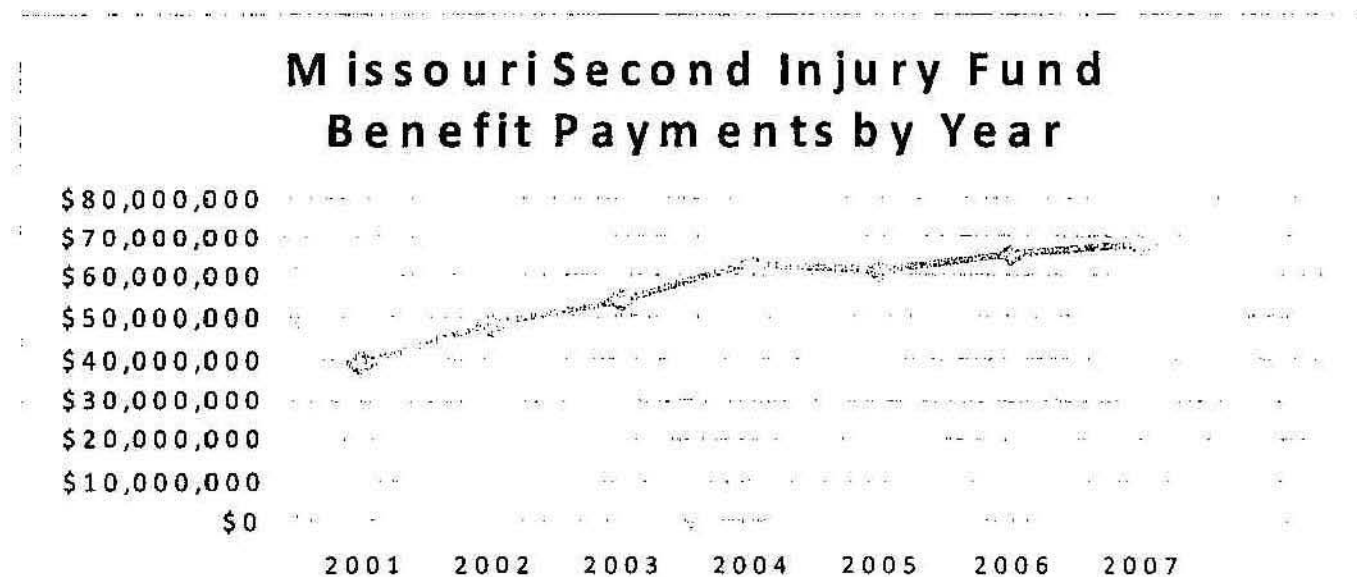


Missouri Second Injury Fund  
Expenditures by Calendar Year by Agency

	2001	2002	2003	2004	2005	2006	2007
Office of the State Treasurer - Operations	\$34,641	\$40,246	\$42,314	\$47,381	\$33,803	\$41,933	\$43,385
Office of the Attorney General - Operations	\$2,037,930	\$1,865,073	\$1,992,285	\$2,229,653	\$2,645,019	\$2,634,803	\$2,815,808
Office of the Attorney General - Leasing	\$95,513	\$114,458	\$77,821	\$103,939	\$102,876	\$161,504	\$199,490
Office of Administration - Operations	\$567,131	\$1,120,418	\$858,452	\$1,396,029	\$1,494,282	\$1,655,456	\$1,720,232
Office of Administration - Capital Improvements	\$2,078	\$2,272	\$1,588	\$5,722	\$2,566	\$0	
Department of Labor and Industrial Relations							
Benefit Payments	\$39,040,907	\$47,761,439	\$53,937,636	\$62,411,992	\$80,995,159	\$65,021,789	\$67,805,836
Attorney charges, refunds, envelopes and postage	\$428,903	\$542,139	\$1,480,805	\$299,329	\$111,599	\$10,700	\$176,005
Department of Revenue - Operations	\$747,361	\$882,698	\$25,066	\$19,676	\$0	\$0	
<b>Totals</b>	<b>\$42,954,464</b>	<b>\$52,428,742</b>	<b>\$58,415,966</b>	<b>\$66,513,722</b>	<b>\$65,385,303</b>	<b>\$69,526,185</b>	<b>\$72,760,756</b>

Note 1: The Department of Labor and Industrial Relations compiles this information by calendar year.

Note 2: The operating expenditures of the Workers Compensation Division are paid from the Workers' Compensation Administration Fund.



**Missouri Second Injury Fund  
Claims Filed, Dismissed, and Served**

<u>Year</u>	<u>Claims Filed</u>	<u>Claims Dismissed</u>	<u>Claims Served</u>
2001	13255	7273	4626
2002	14199	7765	5177
2003	14157	7435	5218
2004	13882	7912	5642
2005	13363	8225	5616
2006	10591	8824	5621
2007	10983	8799	5334
2008	10202	8475	4930

